DESCRIPTION OF TECHNICAL CORRECTIONS

PROPOSED TO THE

TECHNICAL AND MISCELLANEOUS REVENUE ACT OF 1988, THE REVENUE ACT OF 1987, AND CERTAIN OTHER TAX LEGISLATION

For Consideration

By the

SENATE COMMITTEE ON FINANCE

Prepared by the Staff

of the

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INTRODUCTION

This document,[1] prepared by the staff of the Joint Committee on Taxation, provides a summary description of proposed technical corrections to recent tax legislation. No description is provided for clerical or conforming changes.

Part I of the document describes proposed technical corrections to the Technical and Miscellaneous Revenue Act of 1988 (1988 Act). Part II describes proposed technical corrections to the Revenue Act of 1987 (1987 Act). Part III describes proposed pension technical corrections relating to the Tax Reform Act of 1986, the Omnibus Budget Reconciliation Act of 1986, and the Omnibus Budget Reconciliation Act of 1987 (including the Pension Protection Act). Part IV is a description of an additional technical provision relating to Code section 274.

Effective dates.--Unless otherwise specified in the description, the proposed technical correction provisions are effective as if included in the Act to which the correction is being made.

Revenue effect.--The technical corrections provisions described in this document involve no revenue impact.

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[1] This document may be cited as follows: Joint Committee on Taxation, Description of Technical Corrections Proposed to the Technical and Miscellaneous Revenue Act of 1988, The Revenue Act of 1987, and Certain Other Tax Legislation (JCX-56-89), October 2, 1989.

I. AMENDMENTS TO THE TECHNICAL AND MISCELLANEOUS REVENUE ACT OF 1988

A. Corporate Provisions

1. Method of computing net unrealized built-in gain or loss

For purposes of sections 382, 384, and 1374 the method of computing the amount of net unrealized built-in gain or loss is clarified. Items of income or loss that would be treated as built-in gain or loss if recognized within the recognition period are included in the computation of net unrealized built-in gain or loss, without regard to when or whether such items are actually recognized within the recognition period.

2. Modification of conforming amendment relating to S corporations engaged in banking operations

Prior to the Tax Reform Act of 1986, a corporation could not be an S corporation if the corporation's deductions for bad debts could be taken under the reserve method as a bank (under Code sec. 585) or as a thrift institution (under sec. 593) (Code sec. 1371(b)(2)(B)). The Tax Reform Act of 1986 disallowed the use of the reserve method for bad debts for large banks (Sec. 901(a)(1) of the Tax Reform Act of 1986). As a conforming amendment, the 1986 Act provided that a corporation could not be an S corporation if the corporation was a bank or thrift institution, regardless of whether or not that corporation claimed any deduction for bad debts under the reserve method (Sec. 901(d)(4)(G) of the Tax Reform Act of 1986).

The provision modifies the conforming amendment in the 1986 Act such that corporations would not be eligible to be an S corporation if the corporation could have claimed a deduction for bad debts under the reserve method as a bank if it were a small bank.

3. Reduction in S corporation income taxed to shareholders by the amount of built-in gains tax paid

The provision clarifies that the amount of any built-in gains tax paid by an S corporation reduces the amount of S corporation income that is taxed to the S corporation shareholders.

4. Reduction in built-in gains tax by minimum tax credit carryovers

The provision provides that any minimum tax credit carryover of an S corporation arising from a year the corporation was a C corporation may reduce the built-in gains tax of the S corporation.

5. Determination of tax basis of property transferred to Alaska Native Corporations

The 1988 Act states that no provision in any law (whether enacted before, on, or after the date of enactment of the 1988 Act) shall affect the date on which a transfer to an Alaska Native Corporation is made for purposes of determining basis for Federal tax purposes. The amendment removes any retroactive effect of this provision in the 1988 Act with respect to determining the tax basis of property transferred to an Alaska Native Corporation. No inference is intended regarding the interpretation of such prior law.

B. Minimum Tax Provisions

1. Tax benefit rule

The Tax Reform Act of 1986 provided that the Treasury Department may prescribe regulations providing proper adjustments where the taxpayer will not receive a tax benefit from an item for any taxable year. The provision clarifies that this rule applies whether the tax benefit will result in the current year or in another year.

The provision also provides that the prior law add-on minimum tax rule requiring the Treasury Department to issue tax benefit regulations (sec. 58(h)) was not repealed by the Tax Reform Act of 1986 in so far as it relates to carryovers to taxable years beginning after December 31, 1986.

2. Minimum tax credit

The provision clarifies that the minimum tax credit includes any minimum tax imposed in prior years by reason of the 90-percent limitation on the use of the alternative minimum tax foreign tax credit. This position is consistent with the position taken by the Internal Revenue Service in its forms and accompanying instructions. (Under present law, the minimum tax credit includes any minimum tax previously paid because of the 90-percent limitation on the use of net operating loss deductions.)

3. Treatment of disqualifying dispositions of certain stock

The provision clarifies that the minimum tax rules applicable to a disqualifying disposition of stock acquired pursuant to the exercise of an incentive stock option where the amount realized is less than the value at the time of exercise follows the regular tax rules of section 422A(c)(2) where the stock is disposed of in the same taxable year the income is taken into account for minimum tax purposes. Thus, the amount included in alternative minimum taxable income will not exceed the amount realized on the sale or exchange of the stock over the adjusted basis of the stock.

4. Treatment of acquisition expenses of life insurance companies

In determining adjusted current earnings under the alternative minimum tax, acquisition expenses of life insurance companies are required to be capitalized and amortized in accordance with the treatment required under generally accepted accounting principles, as if such treatment was required for all prior taxable years. The committee report to the bill would clarify that to the extent that life insurance reserves are relevant in determining the

amortization schedule under generally acceptable accounting principles, tax reserves instead of reserves determined under generally acceptable accounting principles are to be used.

C. Accounting Provisions

1. Long-term contracts

a. Percentage of completion method.--In general, a portion (generally, 90 percent) of the items with respect to certain long-term contracts must be taken into account under the percentage of completion method. Under the percentage of completion method, as presently drafted, it is unclear whether all of the income under the contract must be taken into account over the contract term if not all of the total estimated contract costs are actually incurred as of the end of the taxable year in which the contract is completed. The provision clarifies that, except for purposes of applying the look-back method, all of the income under the contract must be taken into account no later than one year after the taxable year in which the contract is completed.

b. Treatment of costs attributable to the installation of integral components to real property.--Present law provides an exception to the long-term contract rules for home construction contracts and more generous treatment for residential construction contracts. The provision clarifies that the cost of installing any integral component to real property (e.g., a heating or air conditioning system) is to be considered a qualifying cost for purposes of the definition of home construction contract and residential construction contract.

c. Exception for certain construction contracts.--Present law provides an exception to the long-term contract rules for certain construction contracts of taxpayers whose average annual gross receipts for the prior three taxable years do not exceed $10 million. The provision clarifies that the gross receipts of any predecessor of the taxpayer (and certain related persons) are to be taken into account in determining whether this exception applies.

d. Treatment of interest under the look-back method.--Upon the completion of a long-term contract, a taxpayer must pay interest under the look-back method to the extent that taxes in a prior contract year were underpaid due to the use of estimated contract price and costs rather than the actual contract price and costs. The provision clarifies that such interest is to be treated as an increase in tax for purposes of subtitle F of the Code (other than the estimated tax provisions).

e. Application of the lookback method to amounts taken into account after completion of the contract.--Present law provides that the lookback method applies if amounts are received or accrued after completion of a long-term contract. In addition, under the lookback method, amounts that are

received or accrued after the completion of a contract are to be taken into account by discounting such amounts to their present value as of the completion of the contract. A taxpayer may elect with respect to any contract not to discount amounts received or accrued after the completion of the contract. The provision clarifies that the lookback method applies if costs are taken into account after the completion of a contract and that costs under a contract are to be discounted in the same manner as items of income.

f. Treatment of certain home construction contracts for purposes of the adjusted current earnings provision of the alternative minimum tax.--In determining alternative minimum taxable income, the amount of income derived from certain home construction contracts by certain small taxpayers is not required to be determined under the percentage of completion method of accounting. The provision clarifies that, in determining adjusted current earnings under the alternative minimum tax, the amount of income derived from such contracts by such taxpayers is not required to be determined under the percentage of completion method of accounting.

g. Application of regulatory authority to certain ship contracts.--The provision clarifies that the regulatory authority granted to the Secretary of the Treasury to prevent the avoidance of section 460 applies to qualified ship contracts.

2. Uniform cost capitalization rules

a. Application of section 189.--Section 189, before its repeal by the 1986 Act, required the capitalization of certain construction period interest and taxes. Such capitalized costs were generally amortized over a 10-year period. Costs were not subject to the rules of section 189 if they were capitalized under section 266. Section 263A, as enacted by the 1986 Act, also requires the capitalization of certain interest and taxes. Under section 263A(f), interest may be capitalized pursuant to a formula that takes into account all prior capitalized costs (the avoided cost method). The provision clarifies that the costs that would have been taken into account for purposes of sections 189 and 266 before the effective date of the 1986 Act will be taken into account for purposes of section 263A(f) after the effective date of the 1986 Act.

In addition, the provision clarifies that certain property that was provided transition relief under the 1986 Act is subject to the capitalization rules of section 189 (as effective before its repeal) with respect to interest and is subject to the capitalization rules of section 263A with respect to other costs, including taxes.

b. Exception for free-lance authors, photographers, and

artists.--The 1988 Act exempted certain free-lance authors, photographers, and artists from the uniform capitalization rules of section 263A. The provision clarifies that the exemption also applies to certain expenses incurred by certain corporations owned by such persons.

c. Exception for certain producers of animals.--Prior to the 1988 Act, producers of certain plants and animals were subject to the uniform capitalization rules unless an election was made to forego the use of accelerated depreciation. The 1988 Act exempted certain producers of animals from the uniform capitalization rules and allowed the revocation of prior elections to forego the use of accelerated depreciation. The provision clarifies that only producers of animals may revoke prior elections.

3. Installment sales

Treatment of sales of personal use property by individuals.--Present law provides that certain installment sales by nondealers are subject to special interest-charge and pledging rules. The provision clarifies that the sale of personal use property by an individual is not subject to these special interest-charge and pledging rules.

D. Foreign Tax Provisions

1. Source rules: Special rules for transportation income

a. The provision exempts from U.S. income tax gross income from the international operation of ships or aircraft derived by an individual resident of a possession, or a corporation organized in a possession, if such possession grants an equivalent exemption to U.S. individuals or corporations. In the case of any possession on the mirror code, the provision clarifies that such reciprocal exemptions exist.

b. The provision clarifies that a foreign corporation may be exempt from U.S. tax on its income from the international operation of ships or aircraft, even if the equivalent tax exemption of the country where the foreign corporation was organized does not extend to dual resident companies that are both incorporated in the United States and also treated as residents of that country under its tax laws.

c. Under the provision, failure to have substantially all of a taxpayer's U.S. source gross transportation income attributable to regularly scheduled transportation (or, in the case of income from the leasing of a vessel or aircraft, attributable to a fixed place of business in the United States) would not automatically prevent transportation income other than U.S. source gross transportation income from being treated as effectively connected with the conduct of a trade or business in the United States if the general rules would treat such other transportation income as so effectively connected.

2. U.S. taxation of income earned through foreign corporations

a. Exceptions for same-country interest, rents, and royalties.--The provision clarifies that the exceptions from treatment as foreign personal holding company income for certain interest received from a related person that is organized in the same country as the recipient, and for certain rents and royalties received from a related person with respect to property within the country of the recipient, apply only to payments received from a related person that is a corporation.

b. Losses of foreign corporations electing to be taxed as domestic insurance companies.--The provision clarifies that any loss of a foreign corporation that makes an election to be treated as a domestic insurance company cannot reduce the taxable income of any other member of its affiliated group.

3. Treatment of foreign taxpayers

a. Partnership withholding.--

i. For purposes of determining the adjusted basis of an interest in a partnership, the provision generally treats withholding tax paid by a partnership on behalf of a foreign partner as a deemed distribution to such partner on the earlier of (1) the date such tax is paid to the Internal Revenue Service, or (2) the last day of the partnership's taxable year for which the tax is paid.

ii. The provision subjects a partnership to an underpayment of estimated tax penalty similar to that applicable to corporations if the partnership fails to properly pay quarterly installments of withholding tax with respect to foreign partners.

b. Excise tax on insurance premiums paid to foreign persons.--The provision conforms the exemption from the excise tax for premiums on life, sickness, and accident insurance policies and annuity contracts with the existing exemption from the tax for premiums on casualty insurance policies and on all reinsurance policies.

4. Foreign currency gain and loss

The provision clarifies that the character of any foreign currency gain or loss is determined under the rules of section 988 notwithstanding other gain and loss characterization rules (e.g., the rule characterizing gain and loss from trading section 1256 contracts) in the Code.

5. Tax-exempt shareholders of DISCs

The provision clarifies that all tax-exempt DISC shareholders that are generally subject to the unrelated business income tax are equally subject to unrelated business income tax on income with respect to DISC stock.

E. Estate and Gift Tax Provisions

1. Rates and unified credit

Phaseout of unified credit for nonresident alien decedents.--The 5-percent phaseout of the unified credit would apply to the estate of an nonresident alien only to the extent that the estate qualified for the credit.

2. Gift tax

a. Marital deduction for gifts made by nonresident alien.--For gift tax purposes, a nonresident alien would receive the same marital deduction allowed a resident alien.

b. Annual exclusion for transfers to alien spouse.--The $100,000 annual exclusion for gifts made to an alien spouse would be allowed only for transfers of nonterminable interests. The provision would be effective for gifts made after date of committee action.

3. Amounts includible in gross estate

Amount included in gross estate when creation of joint tenancy constituted completed gift.--If the creation of a joint tenancy between citizen and noncitizen spouses resulted in a gift prior to July 14, 1988, only a portion of the joint tenancy property would be included in the decedent spouse's estate.

4. Estate tax marital deduction

a. Treatment of survivor annuity as QTIP.--A survivor annuity would be treated as qualifying terminable interest property for purposes of the marital deduction only if includible in the gross estate of the decedent as an annuity.

b. Availability of marital deduction for nonresident alien.--The statute would be clarified to allow property passing from a nonresident alien to an alien spouse to qualify for the marital deduction if passing to a qualified domestic trust (QDT).

c. Availability of marital deduction for property transferred to qualified domestic trust (QDT) before filing of the estate tax return.--Probate property passing to an alien spouse would qualify for the marital deduction if such property is transferred or irrevocably assigned to a QDT before the estate tax return is filed. Estates of decedents dying before the date of enactment would be allowed one year to make such a transfer or assignment.

5. Credit to estates of alien spouses for estate tax paid by estate of decedent spouse

a. Availability of credit to nonresident alien.--The credit for estate tax previously paid by the decedent spouse would be allowed to a surviving spouse who is a nonresident alien.

b. Credit for taxes imposed on qualified domestic trust (QDT) not reduced by amount qualifying for marital deduction.--The credit for the estate tax imposed on property in a QDT would not be reduced to reflect that such property qualified for the marital deduction.

6. Estate tax on qualified domestic trust (QDT)

a. Definition of distribution.--The payment of the estate tax on a QDT itself would be a distribution subject to the estate tax.

b. Multiple QDTs.--If there is more than one qualified domestic trust, the tax rate on each trust would be the highest estate tax rate in effect at the date of the decedent's death unless there is one U.S. citizen or domestic trustee responsible for filing the returns and paying the tax on all qualified domestic trusts.

c. Interest on tentative tax.--The tentative tax refunded upon final determination of estate tax on a QDT would bear interest.

d . Basis for estate tax on lifetime distributions.--The basis of property distributed as corpus from a QDT would be increased by the portion of estate tax attributable to appreciation in such property paid by the trust.

e. Due date for tax on deathtime transfers.--The return for the estate tax imposed on a QDT by reason of the death of the surviving spouse would be due on the same date as the estate tax return for that spouse.

7. Generation-skipping transfer tax

a. Basis adjustment.--The total basis adjustment for property subject to the generation-skipping transfer tax would be limited to its fair market value.

b. Double deduction of expenses.--Administrative expenses would not be simultaneously deductible against both the generation-skipping transfer tax and the income tax.

c. Valuation date for transfers for which gift tax

return not required.--Generation skipping transfers would be valued as of the date of transfer if an allocation of exemption is made on a gift tax return that would be timely filed if such a return were required.

8. Estimated taxes of trusts and estates

Exception from estimated taxes for two years following decedent's death.--If no will is admitted to probate, a grantor trust with primary responsibility for paying taxes, debts and administrative expenses of a decedent would not be required to pay estimated taxes for taxable years ending within two years of the decedent's death.

9. Treaty interaction with estate and gift tax marital deductions

Under the provision, certain estate and gift tax marital deductions available pursuant to treaties to nonresident aliens transferring U.S. property would apply notwithstanding inconsistent 1988 Act provisions.

F. Application of 2-Percent Floor on Itemized Miscellaneous Deductions to Indirect Deductions Through Pass-Through Entities

1. 2-percent floor and pass-through entities

Under present law, the Secretary of the Treasury is required to prescribe regulations prohibiting the indirect deduction through pass-through entities of amounts that would not be deductible under the 2-percent floor on miscellaneous itemized expenses if paid or incurred directly by an individual. In the 1988 Act, Congress intended to exclude a shareholder's share of expenses of publicly-offered mutual funds from the 2-percent floor until December 31, 1989. Instead, the 1988 Act inadvertently sunset the entire prohibition for taxable years beginning after that date. Under the correction, the prohibition on indirect deduction through pass-through entities would be made permanent. The exclusion for shareholder expenses of publicly-offered mutual funds would remain permanent.

G. Insurance Provisions

1. Treatment of modified endowment contracts

a. Treatment of qualified additional benefits.--The provision clarifies that an increase in the charge for a qualified additional benefit is not a material change in the benefits under a contract, and, consequently, the 7-pay test is not to be reapplied at such time. An addition of, or an increase in, a qualified additional benefit, however, is to be considered a material change in the benefits under the contract and requires a reapplication of the 7-pay test.

b. Increase in benefits based on cost-of-living index.--The provision clarifies that, to the extent provided in regulations, a material change does not include any cost-of-living increase based on an established broad-based index if the increase is funded ratably over the remaining period during which premiums are required to be paid under the contract (rather than over the remaining life of the contract).

c. Treatment of contracts with a negative 7-pay premium.--The committee report to the bill would clarify that a contract which is materially changed is not to be considered a modified endowment contract if the calculation of the 7-pay premium after the material change is a negative amount provided that no additional premiums are paid during the first 7 years after the material change.

d. Timing of death benefit increases under the material change rules.--The committee report to the bill would clarify that a death benefit increase that occurs before the payment of a premium that is not necessary to fund the lowest death benefit payable during the first 7 contract years may be considered a material change in the benefits provided under a contract, and, in such case, the material change would be considered as occurring on the date that such premium is paid.

e. Aggregation rules for modified endowment contracts and annuity contracts.--The provision clarifies that contracts under qualified pension plans are not subject to the aggregation rules which generally apply to modified endowment contracts and annuity contracts. In addition, the provision clarifies that the aggregation rules are to apply only to contracts issued by the same company (or related companies) to the same policyholder during any calendar year.

f. Special effective date provision where death benefit increases by more than $150,000.--The committee report to the bill would clarify that if the death benefit under a contract increases by more than $150,000 over the death benefit under

the contract as of October 20, 1988, then the contract would be subject to the material change rules as of the date that the death benefit exceeds the threshold. In addition, the committee report would provide that in determining whether the death benefit increase constitutes a material change, the death benefit payable under the contract as of October 20, 1988, increased by $150,000 is to be taken into account rather than the lowest death benefit payable during the first 7 contract years.

g. Exception to special effective date provision where death benefit increases by more than $150,000.--The provision clarifies that the exception to the $150,000 death benefit increase provision applies to any contract that, as of June 21, 1988, required at least 7 level annual premium payments and under which the policyholder makes at least 7 level annual premium payments.

h. Treatment of contracts that are considered entered into on or after the effective date.--The committee report to the bill would clarify the treatment of an insurance contract that is entered into before June 21, 1988, and that is exchanged on or after such date for another contract or that is otherwise treated under the effective date provisions as entered into on or after such date. The committee report would provide that the 7-pay premium for such a contract is to be reduced by the cash surrender value of the contract in the same manner as a contract that is materially changed.

2. Treatment of certain workers' compensation funds

The provision clarifies that if, for the first taxable year beginning on or after January 1, 1987, a qualified group self-insurers' fund changes its treatment of policyholder dividends to take into account such dividends no earlier than the date that the State regulatory authority determines the amount of the policyholder dividend that may be paid, then such change is to be treated as a change in method of accounting and no section 481(a) adjustment is to be made with respect to such change in method of accounting.

3. Special estimated tax payments

a. Deduction allowed only if tax benefit results.--The provision clarifies that a deduction is allowed for unreversed discount only to the extent that the deduction results in a tax benefit for the taxable year of the deduction or a prior carryback year.

b. Due date of special estimated tax payments.--The provision clarifies that special estimated tax payments are to be made on or before the due date (determined without regard to extensions) for filing the return for the taxable year for which the deduction is allowed.

c. Special loss discount account.--The provision clarifies that any amount added to the special loss discount account must be subtracted from such account and included in gross income no later than the 15th year after the year for which the amount was added to the account.

d. Treasury regulatory authority.--The provision clarifies that the authority granted to the Secretary of the Treasury to prescribe such regulations as may be necessary or appropriate to carry out the purposes of section 847 shall include the authority to prescribe rules that apply in cases where the deduction allowed for any year is less than the unreversed discount as of the close of such year.

e. Effective date.--The provision clarifies that the amount of the deduction for unreversed discount is to be determined by considering losses incurred in taxable years beginning December 31, 1986, rather than losses incurred after December 31, 1986.

f. Earnings and profits.--The provision clarifies that the earnings and profits of any corporation is not to be reduced by the deduction allowed under section 847 for unreversed discount or increased by inclusions required under section 847. For purposes of the alternative minimum tax, however, the adjusted current earnings of a corporation is to be reduced by the deduction allowed under section 847 and increased by the inclusions required under section 847.

g. Section 1503(c) limitation.--The section 847 deduction would be subject to the section 1503(c) limits on losses in consolidation, and the amount of the special estimated tax payments would be determined by taking into account the section 1503(c) limits in consolidation.

H. Pension Provisions

1. Treatment of churches under certain deferred compensation programs

The provision clarifies the exemption from the application of section 457 for church plans. Under the provision, churches would be exempt from the definition of eligible employer.

2. One-time election with respect to elective deferrals

The provision clarifies the regulatory authority in the exception to the definition of elective deferrals (sec. 402(g)(3)) to provide that a contribution is not treated as an elective deferral if, under the salary reduction agreement, the contribution is made pursuant to (1) a one-time irrevocable election made by the employee at the time of initial eligibility to participate in the agreement or (2) a similar arrangement involving a one-time irrevocable election specified in regulations.

3. Effective date with respect to deductibility of certain contributions by self-employed individuals

The provision clarifies that the effective date of the 1988 Act rule relating to the deduction rules for self-employed individuals is effective as if included in the Tax Reform Act of 1986, rather than as if included in the Pension Protection Act of 1987.

4. Deduction for payments relating to standard terminations

The deduction rule relating to employer liability payments treated as contributions to qualified plans is amended to clarify that the rule applies in the case of standard terminations, effective for payments made after January 1, 1986, in taxable years ending after that date.

5. Tax treatment of transfers of interests in individual retirement accounts and qualified governmental plans incident to divorce

Present law permits a transfer of an interest in an individual retirement account (IRA) to be treated as a nontaxable transfer if the transfer is to a former spouse pursuant to a divorce decree. Special tax rules apply under present law to the transfer of an interest in a qualified plan pursuant to a qualified domestic relations order (QDRO). These tax rules do not apply to the transfer of interests in governmental plans and church plans because the QDRO rules do not apply to such plans.

The provision amends the rules relating transfers of interests in an IRA incident to a divorce to conform to the treatment generally of such transfers under the Retirement Equity Act of 1984. The provision permits a transfer of an interest in an IRA to be treated as a nontaxable transfer if the transfer is to a spouse or former spouse under a divorce or separation decree.

The provision applies the same tax rules applicable to transfers pursuant to a QDRO to transfers of interests in a governmental plan or a church plan if the transfer is made pursuant to a domestic relations order as defined in section 414(p)(1) (without regard to sec. 414(p)(1)(A).

The provisions are effective for transfers after the date of enactment in taxable years ending after the date of enactment.

6. Definition of compensation for purposes of IRA deduction limit

Under present law, the maximum deduction limit for contributions to an individual retirement account (IRA) is the lesser of $2,000 or 100 percent of compensation. The provision provides that compensation for this purpose includes the earned income and wages of individuals who are not subject to FICA or SECA taxes because of their religious beliefs. The provision is effective for contributions after the date of enactment.

I. Excise Tax Provision: Undenatured Distilled Spirits

The provision corrects the exemption for educational institutions from the distilled spirits occupational tax to apply to procuring less than 25 gallons of distilled spirits free of tax, instead of specially denatured distilled spirits.

J. Tax-Exempt Bond Provisions

1. Disregard of certain financings in determination of qualification for small-issue exception

The provision amends Code section 148(f)(4)(C)(ii)(II) as enacted by section 6183 of the 1988 Act to clarify that bonds issued by a governmental unit "to make loans to," rather than "on behalf of," other qualifying governmental units do not count in the determination of whether the issuing governmental unit has exceeded $5 million in total annual bond issuance.

2. Application of future legislation to transitioned bonds

The provision clarifies that in the case of any bond to which the amendments made by section 1301 of the Tax Reform Act of 1986 do not apply by reason of any provision of the Tax Reform Act of 1986, any amendment of the 1986 Code (and any other provision applicable to such Code) included in any law enacted after the date of enactment of the Tax Reform Act of 1986 generally, shall be treated as included in section 103 and section 103A (as appropriate) of the 1954 Code with respect to such bond. Exceptions are provided (1) if such law expressly provides that such amendment (or other provision) shall not apply to such bond, or (2) if such amendment (or other provision) applies to a provision of the 1986 Code for which there is no corresponding provision in section 103 and 103A (as appropriate) of the 1954 Code and which is not otherwise treated as included in such sections 103 and 103A with respect to such bond.

The provision is effective as if included in the Tax Reform Act of 1986.

3. Treatment of certain property subject to use restrictions due to financing with qualified 501(c)(3) bonds

The provision clarifies property acquired with the proceeds of qualified 501(c)(3) bonds will be treated as new property for purposes of section 145(d)(2)(A) and, thereby, not subject to the income targeting requirements of section 142(d) in the following two circumstances.

(1) Where the housing is financed by sources other than tax-exempt debt and is later re-financed with tax-exempt debt, the facility is not considered "existing" housing for purposes of section 145(d) if there was a reasonable expectation that the facility would be re-financed with tax-exempt debt and the re-financing with tax-exempt debt occurred within a reasonable period of time thereafter; and

(2) Where the initial financing was with taxable debt because at the time of the taxable financing, State law prohibited tax-exempt financing for the property so financed, then the property will be treated as new property for purposes of a subsequent financing with tax-exempt debt.

K. Research Tax Credit Provision: Election of Reduced Credit

Present law, as amended by the 1988 Act, provides that the section 174 deduction is reduced by 50 percent of the research tax credit determined for the year. Present law permits a taxpayer to avoid a reduction of the section 174 deduction for a taxable year by electing to forgo entirely its section 41 credit for the year. The provision would permit a taxpayer to avoid a reduction of the section 174 deduction by electing to reduce its section 41 credit by the amount of tax saved (assuming the taxpayer is in the highest corporate tax bracket) by not making a reduction of its section 174 deduction. An election by a taxpayer to have this provision apply to a taxable year shall be irrevocable and may be made not later than the time for filing the taxpayer's return for such year (including extensions), except that if the taxpayer's return for a taxable year must be filed before 75 days after the date of enactment of this provision, then the election under this provision may be made at any time before 75 days after such enactment.

L. Low-Income Housing Tax Credit

1. The provision clarifies that students in governmentally supported job training programs, including the Job Partnership Training Act and similar Federal, State or local programs, are deemed to be eligible tenants for purposes of the credit.

2. The operation of the credit in the case of trusts and estates is clarified to provide that the amount of credit and any penalty with respect to the credit is apportioned between beneficiaries and a trust or estate on the basis of the income allocable to each.

3. The provision clarifies that, in the case of a disposition of an ownership interest during the course of a calendar year, the credit is to be allocated pro rata between the seller and purchaser according to the number of days of ownership.

4. In order to carry out legislative intent, the provision authorizes the Treasury Department to issue regulations permitting housing credit agencies to correct administrative errors and omissions with respect to allocations of the credit.

5. The provision clarifies that a person purchasing an interest in a building (including an interest in a partnership owning credit property) steps into the shoes of the previous owner of such interest for purposes of the credit. This provision does not alter the application of the recapture and bond posting requirements as in effect under present law.

These provisions would be effective as if included in the Tax Reform Act of 1986.

II. AMENDMENTS TO THE REVENUE ACT OF 1987

A. Accounting Provisions

1. Installment sales

Present law provides an interest charge on certain deferred tax liabilities arising from certain installment sales. The provision clarifies that such interest is not to be treated as a payment of regular tax for purposes of determining whether the alternative minimum tax applies. Another provision clarifies that the interest charge described in section 453A(c) (relating to nondealer sales) shall be treated as interest for purposes of computing the deductions allowable to a taxpayer.

2. Required payments for certain entities

Partnerships and S corporations may elect a taxable year other than a required taxable year if certain required payments are made. The amount of the required payments generally is phased-in over a 4-year period. The provision clarifies that the phase-in rule is not to apply for taxable years beginning after 1988 unless more than 50 percent of the net income of the partnership or S corporation for the short taxable year that otherwise would have resulted had the election not been made is allocable to partners or shareholders who would have been eligible to include such income over a 4-year period.

B. Corporate Provision:

Adjustments to Earnings and Profits and to Basis of Stock of a Subsidiary

The provision clarifies that the rules requiring certain adjustments to earnings and profits and to the basis of stock of a subsidiary, for purposes of determining gain or loss on disposition of such stock, apply where the corporation disposing of the stock of a former member of an affiliated group is itself a former member of the group. The provision is not intended to apply to the extent such adjustments have already been made with respect to a prior disposition.

C. Vaccine Injury Compensation Trust Fund

The provision would allow funds (not to exceed $6 million annually) from the Vaccine Injury Compensation Trust Fund to be available, as provided in appropriations Acts, for payment of administrative expenses of the National Vaccine Injury Compensation Program.

III. AMENDMENTS RELATED TO OTHER PENSION PROVISIONS

Section 207 of S. 2238, introduced in the 100th Congress by Senators Bentsen and Packwood on March 31, 1988, and reported by the Senate Committee on Finance on August 1, 1988, contains pension-related technical corrections previously approved by the Committee.[2] The technical corrections amend Titles I and IV of the Employee Retirement Income Security Act of 1974 (ERISA) and corresponding provisions of the Internal Revenue Code and the Public Health Services Act. Section 207 of S. 2238 made technical changes to the Tax Reform Act of 1986, the Omnibus Budget Reconciliation Act of 1986, and the Pension Protection Act of 1987.

The proposal would adopt the provisions of section 207 of S. 2238, as previously approved by the Senate Finance Committee with the following modifications and additional provisions.

A. Amendments Related to the Tax Reform Act of 1986

1. Class-year vesting

The Reform Act repealed class-year vesting. The previously-approved technical corrections include a special vesting rule for plans that had class-year vesting so that the elimination of class-year vesting does not adversely affect the vesting status of plan participants. Under the provision, compliance with this special vesting rule would not result in the maintenance of a separate benefit structure for purposes of the minimum participation rule (sec. 401(a)(26)).

2. Time for plan amendments

The Reform Act provided a delayed date for making plan amendments to comply with the provisions of the Act. The previously-approved technicals extend this rule to amendments required by the technical corrections. The provision extends the remedial amendment period to the end of the first plan year beginning after December 31, 1989. As under the original provision, the plan must in any event be operated in compliance with applicable rules.

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[2] For a description of the provisions, see Sen. Rep. No. 100-445, "Technical Corrections Act of 1988", Report of the Committee on Finance, United States Senate, to accompany S. 2238. The pension-related technical provisions were not included in the Technical and Miscellaneous Revenue Act of 1988 as enacted.

3. Health care continuation rules

a. Effective dates.--Certain of the previously-approved technical corrections are effective for plan years beginning after December 31, 1988. At the time the technical corrections were first introduced, this would have been a prospective effective date. Under the provision, December 31, 1988, would generally be changed to December 31, 1989. The effective date for the technical correction relating to termination of continuation coverage in the case of coverage under another group health plan would generally be qualifying events occurring after December 31, 1989. In addition, the provision would apply to individuals who elected continuation coverage in 1989 and who pay for such coverage in accordance with the continuation health care rules.

b. Continuation coverage in the case of Medicare entitlement.--The provision provides that, in the case of a covered employee who becomes entitled to Medicare coverage and continues to be covered by a group health plan, but then terminates employment or suffers a reduction in hours within 18 months following becoming entitled to Medicare, the duration of continuation coverage for the employee's spouse and dependent children is 36 months from the date the beneficiary first became entitled to Medicare coverage. This provision is effective for plan years beginning after December 31, 1989.

The provision would also clarify the present-law rule that if a covered employee has a qualifying event that results in 18 months of continuation coverage, and the covered employee becomes entitled to Medicare coverage before the expiration of the 18 months, any qualified beneficiary who is at that time covered under the group health plan is entitled to continuation coverage for a total of 36 months from the date of the original qualifying event.

B. Amendments Related to the Omnibus Budget Reconciliation Act of 1987 (including the Pension Protection Act)

1. Effective dates of changes relating to amortization periods

The previously-approved technicals provide that the change in the amortization period for experience gains and losses applies to gains and losses established in years beginning after December 31, 1987, and provides a special transition rule for any experience gain or loss determined by a valuation occurring as of January 1, 1988. In Notice 89-52, the Internal Revenue Service provided transitional relief with respect to the effective date of the change in such amortization period. Under the provision, the employer may elect to amortize gains and losses (1) in accordance with the general effective date without regard to the special rule

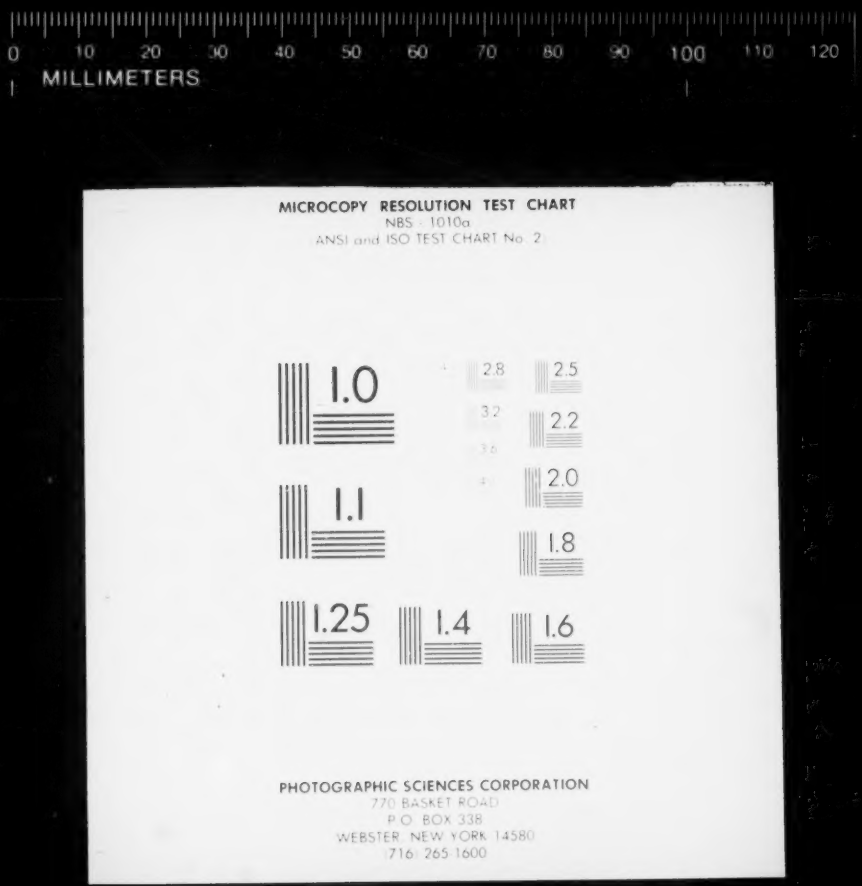
for valuations occurring as of January 1, 1989, (2) in accordance with the special rule, or (3) in accordance with the IRS notice.

C. Miscellaneous

The proposal makes certain clerical changes to the previously-approved technicals, such as correcting incorrect citations and cross references.

IV. ADDITIONAL TECHNICAL: CODE SECTION 274

Under present law, the amount allowable as a deduction for certain expenses for food, beverages, and entertainment is limited to 80 percent of the expense. This 80-percent limitation does not apply to expenses for food or beverages required by Federal law to be provided to crew members of a commercial vessel. The provision would clarify that this exception applies to food or beverages required by any Federal law to be provided to crew members of a commercial vessel.



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